



Do formula-based intergovernmental transfer mechanisms eliminate politically motivated targeting?

GSSP

Evidence from Ghana

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Theories of fiscal federalism imply that determining intergovernmental transfers based on the political incentives results in inefficient allocation of resources across geographic regions. Such practices also can result in tensions between classes, and ethnic and religious groups, which are concentrated in distinct geographical areas. Nevertheless, empirical evidence consistently confirms that the practice of allocating government resources based on political relationships continues to be pervasive around the world. This brief summarizes the results of an IFPRI study in Ghana assessing the effectiveness of formulas as a strategy to limit political motivation behind resource sharing.

Intergovernmental transfers in Africa

In the young democracies in Africa in particular, there is a belief, perpetuated by a history of overt political patronage, that resource allocation is strongly influenced by the nature of the political relationship the receiving group has with higher tiers of government. When there is data available, this belief is supported by evidence. Barkan and Chege (1989) found that in Kenya in the 1980s, budget allocations for construction of new roads and health facilities in President Arap Moi's political strongholds of the Rift Valley and Western provinces were disproportionately high. From 1984 to 1988, between 57 and 68 percent of the road budget each year went to these areas, which held only 33 percent of the country's population. Miguel and Zaidi (2003) showed that in Ghana, annual central government educational expenditure per student in 1998 was 27 percent higher in districts that had voted overwhelmingly for the ruling party in parliamentary elections.

Use of formulas to mitigate political manipulation of transfers

One strategy to counteract this practice has been to place the mandate for distributing national resources with independent agencies. The Finance Commission in India, for example, has had

apparent success in removing political bias as an important consideration in the allocation of resources to regions. ed¹

Another strategy has been the use of formulas to determine resource allocations. This strategy has gained prominence in the developing world after the wave of decentralization in the last two decades. In 1994, Ghana created a pioneering formula-based system of resource allocation through the District Assemblies Common Fund (DACF) that provides the financial sustenance for the local governments of the country. In India, the largest rural development expenditure program, the Sampoorna Grameen Rozgar Yojana (SGRY), launched in 2001, and the 2005 National Rural Employment Guarantee Act (NREGA) that superseded it, are required to devolve resources by means of a formula. South Africa's Local Government Equitable Share, established in 1997, Kenya's Local Authority Transfer Fund, established in 1999, and Nigeria's Federation Account, created in 1999, also use formulas to allocate resources.

How well do formulas work?

The prevailing presumption is that distributing resources by a formula based on economic and welfare variables will suspend the arbitrariness that allows politically motivated targeting. IFPRI researchers in Ghana examined the effectiveness of formulas as a strategy for limiting political

motivations behind resource sharing by studying whether and how a district's transfers from the DACF over the period 1994 to 2005 were influenced by its political characteristics. DACF transfers allow voters to perceive the benefits of having a particular political party in office at the central level, as politicians can manipulate districts' allocations. Transfers from the fund constitute the largest source of financing for local government in Ghana and any political bias in the allocations is unlikely to be offset by other government grants. Examining the influence of politics on DACF transfers can provide insights into the scope of political considerations in allocations that result from other formula-based programs.

There is a debate among researchers about how transfers are affected by the political characteristics of the recipient groups. In one school of thought, transfers will be targeted to districts with relatively more 'swing voters'.ⁱⁱ The main assumption is that voters are willing to compromise their political party preferences if presented with economic benefits from another party. In contrast, another group of researchers argue that voters respond more strongly to economic incentives provided by the political party they prefer.ⁱⁱⁱ The prediction under this "core supporter" model is that politicians, are risk-averse, and, will target more resources to areas where they have concentrated political support to assure the best return in terms of votes.

Researchers who have studied allocation and voting results have found varied evidence. Case (2001) found that block grants to districts in Albania increased with the president's vote share in the previous election. On the other hand, Cole (2009) finds that Indian state governments supplied more subsidized agricultural loans in election years to districts in which they had a narrow margin of victory or loss suggesting that swing voters were targeted. Dahlberg and Johansson (2002) determine that municipalities with swing voters were favored in the award of temporary grants in Sweden.

Research findings in Ghana

Despite being determined by a uniformly applied formula, the study found evidence of political

incentives in the determination of DACF allocations and disbursements to districts. The researchers found that districts with lower vote margins between the two dominant political parties in the previous presidential election receive higher DACF allocations and disbursements. This suggests that the DACF transfers were targeted to swing voters.

The evidence that a district's formula-based allocation is influenced by its political characteristics implies that the formula itself is politically biased. The DACF formula is chosen by a fund administrator and voted into law by parliament. However, the administrator is appointed by the president and the president, through the administrator, has informal agenda-setting powers over the formula recommended to the parliament as well as the ability to reward or punish parliamentarians based on their votes. Within this structure, the president can advance a formula that produces allocations that are in line with his targeting goals. The DACF formula was changed in each of the years under study except in 1995. The study found that the formula changes tended to benefit districts that had lower vote margins in the previous elections.

Conclusions

IFPRI research results found that governments in Ghana can achieve sophisticated political targeting even within the confines of the supposedly unbiased, formula-based sharing rules of the DACF. It shows that resource allocation by means of a uniformly applied formula grounded in economic variables does not necessarily prevent politically motivated targeting. The structures of a formula based-system, such as who determines the formula, and how and when the formula can be altered, are important determinants of how well it works to prevent political manipulation.

ⁱ Khemani, S., 2007. Does delegation of fiscal policy to an independent agency make a difference? Evidence from intergovernmental transfers in India. *Journal of Development Economics* 82, 464-484.

ⁱⁱ Lindbeck, A. and Weibull, J., 1993. A Model of Political Equilibrium in a Representative Democracy. *Journal of Public Economics* 51 (2), 195-209.

Dixit, A. and Londregan, J., 1998. Ideology, Tactics, and Efficiency in Redistributive Politics. *Quarterly Journal of Economics* 113 (1), 497-529.

ⁱⁱⁱ Cox, G., and McCubbins, M., 1986. Electoral Politics as a Redistributive Game. *Journal of Politics* 48 (2), 370-389.

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